

ce Bq
Blup

PRIME MINISTER

DOCKLANDS LIGHT RAILWAY: EASTERN EXTENSION

1. We are to have a further discussion in E(A) on Monday on the basis of a note by Nicholas Ridley. In that he draws out our two major concerns which stand in the way of my giving consent for the Bill to be deposited:

i. the heightened exposure of the Government to pressures for a substantial increase in public expenditure - up to £125m (present prices) - for the Eastern Extension, and even if a source of private funding were found, the acceptance of risk by the Government to meet any shortfalls;

ii. the risk of a direct and adverse impact on the satisfactory conclusion of negotiations with the Canary Wharf Consortium on the funding of the City Extension which the letter of comfort from the Consortium, promoted by the LDDC, does not entirely allay.

2. I need to draw to your attention two further factors which bear on the assessment of these risks. First, the provisional agreement with the Consortium reached last year was based on a contribution to the City Extension equivalent to £45m in Net Present Value terms. On the estimates then available this was sufficient to secure the required 5 per cent real rate of return on the public sector's share of the cost. But this was predicated on the patronage and revenues which would be generated if the Canary Wharf Development proceeded to the planned levels. For that reason enforceable guarantees from the Consortium that their development will

CONFIDENTIAL

proceed to the required scale and timetable are being sought. This is being strongly resisted by the Consortium in the current negotiations and is not a matter on which their letter gives comfort.

3. The second factor arises from cost escalation on the City Extension. The latest estimates produced by LRT in the light of tenders they have recently received indicate an increase of nearly £20m since March. We will need to give separate consideration to this as it is not provided for within LRT's existing External Financing Limit. The railway is now unlikely to generate the required rate of return on a purely financial basis, though it should still meet our investment criteria in cost-benefit terms. There is little prospect of successfully negotiating an increased contribution from the Consortium to cover this financing gap. And it exemplifies the sort of public expenditure risk we face if we now agree to the Bill for the Eastern Extension.

4. In these circumstances it is all the more important that the Consortium deliver their financial contribution in full, as well as the enforceable development guarantees which are being sought. We remain exposed on the latter and possibly on the former too, notwithstanding the letter of comfort which significantly is expressed in cash terms rather than NPV terms (the calculation of which is currently a point of contention).

5. In all the circumstances I feel bound to conclude that consent to the deposit of the Bill should not be given now, especially as we have the possibility of using the late bill procedure.

6. I am copying this minute to Nicholas Ridley, to other members of E(A), and to Sir Robert Armstrong.

R. A. Allan
(Private Secretary)

for J.M.

21 November 1986

(Approved by the Secretary of State for Transport + signed in his absence.)

CONFIDENTIAL

